The Minnesota ALJ, after an exhaustive review of evidence before him,[348] concluded that Qwest had not established compliance with section 272(b)(3), finding:

> The arrangement of officers and directors created by Qwest goes beyond the common reporting of officers to a single superior outside of the particular corporate entity. The directors and officers of both the Qwest BOC and QCC are integrated within each company and the officers and directors of each company are integrated into the corporate structure of the common parent. Some of these same individuals have provided management between the Qwest BOC and its 272 Affiliate by contract. This structure defeats the purpose of the separate officers and directors requirement.

Minnesota ALJ Findings ¶ 60; *accord* Selwyn Minnesota Aff. ¶¶ 51-59.[349] Nothing in Qwest's submission here undermines this finding. Indeed, Qwest's submission raises still more questions that Qwest does not even attempt to answer. For example, Qwest acknowledges that employees of the BOC and section 272 affiliate maintain offices on the same floor of the same buildings, without attempting to show that this close physical proximity is reasonable and appropriate under section 272(b)(3).[350] Similarly, Qwest acknowledges that a large number of employees ("fewer than 200") were transferred between the BOC and section 272 affiliate "during the 272 transition period," without any further explanation as to who these employees are, what positions they held, or otherwise identifying any agreements between the BOC and affiliate concerning their transfer.[351] Much more needs to be known about such employee transfers before a finding of compliance with section 272(b)(3) can be made, because, as the Minnesota ALJ found, [t]here is

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[347] *See* Schwartz Decl. ¶ 53. Even on this narrow fact issue Qwest's application is deficient, as the information presented on employee payrolls for Qwest and QCC concerns a single review that was conducted over a year ago, in March 2001. *Id.* ¶ 53.

[348] *See* Minnesota ALJ Findings ¶¶ 39-61.

[349] *See also* Skluzak Minnesota Aff. ¶¶ 45-54 (attachment 9, hereto). The Minnesota ALJ's approach and findings are strongly supported by the review mandated by the Biennial Audit Procedures, which require an independent auditor to gather employee-specific information on each employee transferred between the BOC and section 272 affiliate, including their use and access to confidential information from their prior employer. *See* Skluzak Minnesota Aff. ¶ 47; Biennial Audit Procedures, Objective III, Procedure 5.

[350] *See* Schwartz Decl. ¶ 55(2).

[351] *See* Schwartz Decl. ¶ 56.

legitimate concern over employee transfers as a means of evading the separate employee requirement."[352] Finally, Qwest recites no policy and presents no evidence concerning the structure of employee reporting and supervision; Qwest cannot maintain an integrated workforce of BOC and section 272 affiliate employees, with Qwest employees reporting to BOC supervisors and BOC employees reporting to Qwest supervisors, and claim "separation" under section 272(b)(3) through the simple expedient of maintaining separate payrolls, publishing generic service-agreements, and using employer-identifying nametags. On this record, Qwest has not established compliance with section 272(b)(3).

C. Qwest Does Not Meet The 272(b)(5) Requirement That All Transactions With the Section 272 Affiliate Be At Arm's Length, Reduced To Writing, And Publicly Available.

Section 272(b)(5) requires that "all transactions" between Qwest and its section 272 affiliate be "on an arm's length basis with any such transactions reduced to writing and available for public inspection." Qwest is not currently in compliance with these requirements, and does not show that it will be in compliance if interLATA authority is granted.[353]

First, as the Minnesota ALJ found, the transactions between Qwest and QCC cannot be deemed at "arm's length" because both entities depend on their joint parent, QSC, to provide legal, public policy, and financial services for these transactions. Minnesota ALJ Findings, ¶¶ 78-80. As the ALJ reasoned: "Entities dealing with each other cannot depend upon the same source for legal services, public policy analysis, and financial consulting with respect to transactions occurring between the two entities and remain at "arm's length" in a transaction." *Id.* ¶ 79. Qwest presents no evidence in its application to dispute this finding, or to explain how

[352] *Minnesota ALJ Findings* ¶ 54.

[353] *See* Minnesota ALJ Findings ¶¶ 74-101; Selwyn Minnesota Aff. ¶¶ 38-50; Skluzak Minnesota Aff. ¶¶ 55-121.

this transaction structure can be deemed consistent with their arm's-length transactions obligations.[354]

Second, although acknowledging that a significant number of employees have been transferred between Qwest and QCC, *e.g.* Schwartz Decl. ¶ 56, no evidence appears in Qwest's application (or on its Internet site) to suggest that the agreements to transfer such employees ever were reduced to writing or that these employee transfers were conducted on an arm's length basis. Plainly, Qwest and QCC cannot engage in coordinated, planned employee transfers without meeting each of the section 272(b)(5) requirements. Such employee exchanges are of special concern because of the substantial "built-in" value offered by employees with substantial specialized training and confidential information.[355] Qwest has not established that it ever intends to comply with section 272(b)(5) concerning such employee transfers, let alone established that it is currently in compliance.

Finally, Qwest has on numerous past occasions failed properly to reduce covered transactions to writing and make them publicly available.[356] Qwest acknowledges many of these past errors, but promises that the circumstances that led to these problems have since been corrected.[357] Yet the Minnesota ALJ has cited numerous *current* instances where Qwest has failed to meet its reporting obligations under section 272(b)(5).[358] At the very least, given Qwest's admitted past noncompliance and the Minnesota ALJ's findings of current

[354] Moreover, as the Minnesota ALJ points out, the failure to engage in arm's-length transactions can seriously damage competition, because, for example, transaction pricing for a BOC and section 272 affiliate ultimately has a net zero effect on the financial returns to their joint owner, but has a serious impact on competing carriers because of the section 272(c) obligation to offer the same terms to competitors. *See* Minnesota ALJ Findings ¶¶ 83-84.

[355] In recognition of the value of such employee transfers, the "California PUC adopted a 25% 'employee transfer fee' to be applied against the annual salary of any Pacific Bell employee that is transferred to an affiliate." Selwyn Minnesota Aff. ¶ 51 (citing California Public Utilities Commission, D.87-12-067, 27 CPUC2d 1, 136).

[356] *See* Skluzak Minnesota Aff. ¶¶ 58-59, 97, 100.

[357] *See* Schwartz Decl. ¶¶ 19-20, 49.

[358] *See* Minnesota ALJ Findings ¶¶ 94-101.

noncompliance, Qwest must be compelled to submit substantial detailed evidence of its compliance with section 272(b)(5). Qwest has not come close to making such a showing in its current application, which devotes little time or effort to establishing section 272(b)(5) compliance and ignores the ALJ's findings.[359]

D. Qwest Has Not Demonstrated Compliance With Its Nondiscrimination Obligations Under Section 272(c).

Section 272(c)(1) "requires that a BOC in its dealings with its section 272 affiliate 'may not discriminate between that company or affiliate and any other entity in the provision or procurement of goods, services, facilities, and information, or in the establishment of standards.'"[360] Qwest has not demonstrated compliance with this nondiscrimination requirement.

First, as the Minnesota ALJ found, Qwest has not established that the exchange of confidential information between Qwest and QCC complies with this nondiscrimination requirement.[361] Qwest claims that the use of confidential information by employees transferred between Qwest and QCC is prohibited, and suggests that access to such confidential information is just as restrictive for employees of Qwest or QCC as it is for employees of a competing carrier.[362] But Qwest ignores the fact that substantial confidential information is shared with, and inevitably used by, Qwest affiliates that provide substantial joint services for both Qwest and QCC. Qwest describes no restriction on the availability of such Qwest or QCC confidential information indirectly through affiliate personnel who provide services to both Qwest and

[359] *Cf. Second Louisiana 271 Order* ¶ 335 (BOC must "provide adequate assurances or demonstrate that it makes publicly available all transactions ... as required by section 272(b)(5) and the Commission's rules").

[360] *Second Louisiana 271 Order* ¶ 341 (quoting § 272(c)(1)).

[361] Minnesota ALJ Findings ¶¶ 105-06.

[362] *See* Schwartz Decl. ¶ 57; Brunsting Decl. ¶ 30(f).

QCC.[363] Indeed, Qwest does not even acknowledge a legal obligation to preclude such indirect use of confidential information. Qwest cannot meet its burden of proof regarding section 272(c) on this record.

Second, Qwest acknowledges that it provides a mechanism for its section 272 affiliate to request a new product, service, or information from Qwest, *see* Schwartz Decl. ¶ 79 & MES-272-13, but describes no similar mechanism being available to competing carriers. Thus, a procedure is in place for QCC to request new products and services, but other IXCs have no similar avenue for requesting new products or services, and instead must wait for Qwest to decide to provide a product or service to QCC before they also would be made available to AT&T. This procedure is discriminatory on its face, in violation of section 272(c).

Third, again as found by the Minnesota ALJ, the evidence presented in that proceeding showed that Qwest failed "to charge late payment fees to the 272 Affiliate in the same manner as late fees are charged to other IXCs," and thus constituted a violation of section 272(c)'s nondiscrimination requirements.[364] Qwest's application here does not respond to this issue. Instead, Qwest vaguely notes its right to charge QCC for late payments, and notes that "interest charges have been recorded," without submitting evidence that such late payments were collected (or, in the alternative, that late payments were similarly not collected from competing IXCs).[365]

Finally, because of the lack of information provided by Qwest concerning its joint marketing work on behalf QCC concerning "planning" services, no finding can be made that the joint marketing efforts (admittedly not made available to competing IXCs) are exempted from

[363] *See* Minnesota ALJ Findings ¶ 106.

[364] Minnesota ALJ Findings ¶¶ 72-73, 108.

[365] *See* Schwartz Decl. ¶ 19; Brunsting Decl. ¶ 41.

compliance with section 272(c).[366] Qwest thus has not established compliance with section 272(c).

E. Qwest Has Not Presented Any Evidence To Establish Compliance With The Joint Marketing Restrictions Of Section 272(g).

Qwest presents no evidence to establish compliance with its joint marketing obligations under section 272(g). Instead, Qwest simply parrots the requirements of the statute, and promises compliance. Such a total absence of evidence cannot meet Qwest's burden of proof, especially in light of the fact that the Minnesota ALJ specifically found Qwest had *not* established compliance with section 272(g).[367]

For example, section 272(g)(1) bars a section 272 affiliate from marketing or selling the BOC's telephone exchange services "unless that company permits other entities offering the same or similar service to market and sell its telephone exchange services." As "proof" of compliance, Qwest simply states that "QCC will not" engage in such marketing or selling, Brunsting Decl. ¶ 49; *see* Schwartz Decl. ¶ 95, without either (i) affirmatively stating whether QCC currently does or does not sell and market Qwest's services, or (ii) if it does currently market such services, identifying the relevant applicable "arms length" agreements and showing that other outside companies have the same opportunities. Qwest makes no attempt to answer these questions, and thus cannot be found to satisfy section 272(g)(1).

Similarly, although Qwest makes clear its intention jointly to market QCC's services if its application is approved, *e.g.*, Schwartz Decl. ¶ 97, and the Minnesota ALJ noted that Qwest had then already billed QCC over $500,000 for joint-marketing "planning" services, *see* Minnesota ALJ Findings, ¶ 116, Qwest presents no evidence to show that the planned joint marketing will be conducted in compliance with section 272(g) and the *Non-Accounting Safeguards Order*.

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[366] *See* Minnesota ALJ Findings ¶¶ 108, 117.

[367] *See* Minnesota ALJ Findings ¶¶ 109-131; *see also* Skulzak Minnesota Aff. ¶¶ 150-159.

For example, Qwest does not even acknowledge, let alone promise compliance with, its obligation under section 251(g) to satisfy equal access requirements in any marketing efforts.[368] Although the Commission has found that a BOC need not submit proposed marketing scripts in order to show compliance with section 272(g), *South Carolina 271 Order* ¶ 236, it has never suggested that an applicant need present *no* evidence other than paper promises. Such evidence, if it exists, should be readily available to Qwest and not difficult to compile and present. For example, training materials concerning such joint marketing efforts could be submitted. If no written training materials are available, then Qwest could submit a description of what training was provided, to whom, and over what period of time.[369]

Finally, Qwest and QCC, although they appear already to have engaged in substantial planning and preparation for joint marketing of QCC's services, provide no evidence of what has been entailed in such work in order to show that it has been (and will be) consistent with the requirement that such "joint marketing" not include "BOC participation in the planning, design, and development of a section 272 affiliate's offerings."[370] Again, Qwest's simple pledge that it will not participate in such conduct is insufficient, especially in light of the broadly worded joint marketing agreement between it and QCC[371] and the fact that Qwest just last summer

[368] *See Non-Accounting Safeguards Order*, ¶ 292.

[369] AT&T describes such training materials and information as examples only, and does not intend to suggest that such materials could alone satisfy a BOC's burden in this area. Moreover, the minimal training materials that were submitted by Qwest are woefully inadequate to establish that Qwest will satisfy section 272(g). These materials include only a one-paragraph summary description of the joint marketing provisions, and do not even mention the equal access obligations. *See* Brunsting Decl. Exhibit JLB15 272

[370] *Non-Accounting Safeguards Order* ¶ 296.

[371] The Minnesota ALJ noted that, in the then-existing joint marketing agreement, Qwest committed to help with, among other things, "planning sales and promotion functions," but no Qwest witness was able to describe what was involved in the "planning functions." Minnesota ALJ Findings ¶¶ 113-115.

indisputably engaged in illegal marketing of QCC's services, only later to explain it "occurred under a mistaken interpretation of the application of the Act."[372]

On this record, no finding can be made that Qwest has and will meet the marketing requirements of section 272(g).

In sum, Qwest and its section 272 affiliate have not met their burden of showing that they will operate in accordance with section 272 if granted in-region interLATA authority. This application may be rejected on that basis alone.

VI. QWEST'S ENTRY INTO THE INTERLATA MARKET IS NOT CONSISTENT WITH THE PUBLIC INTEREST.

Even if the Commission could find that Qwest had fully implemented its obligations under the competitive checklist, the record here precludes any finding that granting Qwest's application is consistent with the public interest. At the heart of the public interest inquiry, as Congress conceived it and as this Commission has explained, is a determination of whether, notwithstanding checklist compliance, the local market is in fact fully and irreversibly open to competition. Because the Commission cannot make this determination in Qwest's five states, a grant of section 271 authority is premature and wholly at odds with the fundamental premise of the Act.

A. InterLATA Authorization Is Not In The Public Interest Unless The BOC's Local Markets Are Irreversibly Open To Competition.

In Qwest's view, the Commission should virtually presume that the public interest will be served by granting Qwest's application, because (in Qwest's view) such approval will spur competitors to enter the local market. Any such presumption, however, would conflict directly

[372] Minnesota ALJ Findings ¶ 125. Specifically, in July 2001, Qwest ran advertisements in Minnesota newspapers promoting QCC's performance in a consumer satisfaction survey, and the Minnesota ALJ found that "the advertisements and scripts used by Qwest demonstrate that Qwest was engaged in joint marketing activity of the Qwest BOC and its 272 Affiliate prior to Qwest's entry into the interLATA market." Minnesota ALJ Findings ¶ 123; *see also* Skluzak Minnesota Aff. ¶ 156.

with the plain language of the statute, which puts the burden on the applicant to show that its entry would be "consistent with the public interest;" the Commission has flatly rejected the argument that the public interest test can be satisfied by simply presuming that the benefits of entry into long distance will outweigh competitive harms from premature authorization.[373]

In fact, the absence of any meaningful local competition is itself a compelling reason to reject an application as inconsistent with the public interest.[374] The lesson from experience in Texas is clear: allowing an incumbent LEC to provide interLATA services before local markets are open will not spur successful local competition.[375] If CLECs cannot profitably offer local residential service to customers, they cannot and will not effectively compete in local markets, regardless of whether the incumbent has obtained long-distance authorization.[376]

Accordingly, as the Commission has recognized, granting Qwest's request for long distance authority can serve the public interest only if the Commission finds that the BOC's

[373] *See Michigan 271 Order* ¶ 43 ("Section 271 places on the applicant the burden of proving that all of the requirements for authorization to provide in-region, interLATA services are satisfied"); ¶ 388 ("As we have previously observed, 'the entry of the BOC interLATA affiliates into the provision of interLATA services has the potential to increase price competition and lead to innovative new services and marketing efficiencies.' Section 271, however, embodies a congressional determination that, in order for this potential to become a reality, local telecommunications markets must first be open to competition so that a BOC cannot use its control over bottleneck local exchange facilities to undermine competition in the long distance market. Only then is the other congressional intention of creating an incentive or reward for opening the local exchange market met.")

[374] *See Sprint* v. *FCC*, 274 F.3d 549 (D.C. Cir. 2001).

[375] Although Qwest boasts (Br. at 179-80) of competition currently being provided by Texas CLECs, the January 2001 *TPUC Report* on the "Scope of Competition in Telecommunications Markets of Texas" reveals that "monopoly power exists . . . in residential and rural markets in Texas" (*id.* at 83; *see* xiii) and severe financial problems have caused both large and small CLECs to reduce or eliminate their residential service in Texas (*id.* at 55-58, 80-81). The Report also reveals that the lack of competition has permitted SWBT to extend its monopoly into the provision of bundled combinations of local and long distance services, and to *raise* its prices for local services to both residential and business customers. *Id.* at x, 62-64, 79, 81). In sum, the TPUC concludes: "By the end of 2000, SWBT's financial position had strengthened relative to the CLECs. *SWBT's entry into the long distance market has weakened the ability of CLECs to challenge SWBT in local voice service*. *Id.* at 81 (emphasis added).

[376] Emboldened by its ability to market bundles of local and long distance services without any competition, in February, 2001, SWBT *raised* its residential long distance rates in Texas by 10 to 33 percent, *increased* its basic rates for long-distance service by more than 10 percent, and *also increased* the "discounted rate" for customers who buy other services from SWBT by 33 percent. "SWBT Raises Nonlocal Call Rates: Company Says Prices Better Reflect Costs," *The Dallas Morning News*, February 2, 2001.

"local market is open and will remain so."[377] As the Commission has likewise recognized, no such finding is possible if the "BOC has engaged in discriminatory or other anticompetitive conduct, or failed to comply with State and federal telecommunications regulations," because the provisions of the 1996 Act that are directed at opening the local exchange market "depend, to a large extent, on the cooperation of incumbent LECs, including the BOCs, with new entrants and good faith compliance by such LECS with their statutory obligations."[378] While the Commission has stated that it "will not withhold Section 271 authorization on the basis of isolated instances of allegedly unfair dealing or discrimination," it has indicated that it will take such action where, as here, "a pattern of discriminatory conduct" exists that undermines its confidence that the relevant "local market is open and will remain so" after the grant of Section 271 authority.[379]

B. Qwest Has Engaged In A Pattern Of Anticompetitive Acts And Violations Of Sections 251, 252 and 271 Of The Act To Maintain And Expand Its Market Power Over Local Service.

Qwest has failed "to cooperate in opening its network to competitors" and instead has engaged in a pattern of "discriminatory and other anticompetitive conduct" that precludes any finding that Qwest's local markets are open to competition and will remain open if Qwest receives the requested interLATA authority. Over the past five years, Qwest (and its predecessor US WEST) have undertaken a pervasive effort to forestall competition in its local exchange markets at the same time that it launched its efforts to provide service across LATA boundaries. These ongoing anticompetitive and unlawful actions conclusively refute Qwest's claim that it is, and will remain, committed to "accelerat[ing] and complet[ing] the process of opening its local markets to competition."[380]

[377] *See SBC Texas 271 Order* ¶ 431.

[378] *Michigan 271 Order* ¶ 397.

[379] *See Michigan 271 Order* ¶¶ 391, 397; *SBC Texas 271 Order* ¶ 431; York 271 Order ¶ 431, 444.

[380] Application at 2.

1. Qwest's Violations of Section 252 (Secret Interconnection Deals).

As demonstrated above, Qwest has undertaken a deliberate, region-wide scheme to violate its nondiscrimination obligations under the Act by violating Section 252 and conspiring to confer secret, favorable interconnection "deals" on selected CLECs. In some of these secret interconnection arrangements, Qwest has silenced its CLEC competitors, securing their acquiescence to a prohibition on their participation in the proceedings evaluating Qwest's compliance with its requirements under Section 271. Qwest concealed these interconnection agreements from the state commissions, rather than file them as the Act requires, to prevent other CLECs (and the state commissions) from becoming aware of the favorable interconnection terms and conditions that were not being made available to other CLECs.

This pervasive anticompetitive practice has now been the subject of actions by several independent state authorities, including Iowa, Arizona and Minnesota. The Iowa Utilities Board found that Qwest had violated section 252 of the Act and section 38.7(4) of the Iowa Code by failing to file three interconnection agreements in a timely manner.[381] The Board ordered Qwest to identify and file any other interconnection agreements that are effective within Iowa, providing sixty days for compliance with this mandate.[382] The staff of the Arizona Corporation Commission ("ACC") confirmed the obviousness and seriousness of Qwest's section 252 violations and anticompetitive conduct in a report released on June 7, 2002, which recommended that Qwest be required to file 25 secret agreements.[383] The staff has also recommended a significant assessment of fines for the failure to file these agreements, and explicitly

[381] *AT&T Corp. v. Qwest Corporation, Order Making Tentative Findings, Giving Notice For Purposes Of Civil Penalties, And Granting Opportunity To Request Hearing*, Docket No. FCU-02-2, May 29, 2002, at 16 (Attachment 8 hereto).

[382] *Id.* at 17; *see supra* at 21-23 (discussing Iowa findings of Section 252 violation and discrimination).

[383] *Staff Report And Recommendation In The Matter Of Qwest Corporation's Compliance With Section 252(e) Of The Telecommunications Act of 1996*, Docket No. RT-00000F-02-0271, at 17-18 (Attachment 4 hereto).

recommended a higher forfeiture for seven agreements that "contained clauses *prohibiting* the carrier or CLEC from participating in a state regulatory proceeding" because of "the more egregious nature of the infraction."[384] Qwest's unlawful conduct also is under investigation in other states, including New Mexico, Washington, and Minnesota, where the Minnesota Department of Commerce is seeking to have millions of dollars of sanctions imposed against Qwest.[385]

AT&T demonstrated above that Qwest's secret, discriminatory agreements preclude any reasoned finding that Qwest satisfies the competitive checklist. These agreements also preclude a finding that Qwest's application is in the public interest for two independent reasons. First, Qwest's practice of entering into and concealing these interconnection arrangements violates section 252 of the Act, and directly impairs the development of a competitive local exchange market. Qwest's discriminatory provision of interconnection and network elements on preferential terms to some CLECs but not others has a direct and obvious inhibiting impact on the development of a competitive local exchange market. Qwest's deliberate concealment of these agreements from state regulators and CLECs then exacerbated this problem because regulators could not take action against these discriminatory agreements and potential entrants were unaware of the availability of terms and conditions offered to their competitors.

Second, provisions in several of these secret agreements prohibit the participation of necessary parties in the proceedings concerning Qwest's application for section 271 authority and therefore raise serious public interest concerns. As the ACC staff concluded, "agreements which attempt to suppress participation by all parties for full development of the record in

[384] *Id.* at 18-19 (emphasis in original); *see supra* at 24-25 (discussing findings in Arizona).

[385] *See supra* at 19-20 (discussing Minnesota proceeding, discriminatory concealment of preferential treatment on rights of way and other terms).

regulatory proceedings before the Commission are not in the public interest."[386] As the ACC Staff correctly recognized, the critical role of state commission section 271 proceedings is wholly undermined if the efficacy of these proceedings is cast into doubt. Similarly, the Commission's section 271 approval process is a meaningless exercise if parties with relevant information are silenced or excluded. Granting Qwest's application in the face of these grave concerns about the fundamental integrity of the approval process cannot be in the public interest.

2. Qwest's Violation of Section 251 (Refusal To Test UNE-P Services).

At the same time that Qwest has concealed discriminatory interconnection arrangements and purchased CLEC silence in state section 271 proceedings, it has engaged in unlawful efforts to avoid its interconnection obligations, with at least one of these derelictions resulting in an adverse finding by a state commission. On April 9, 2002, the full Commission of the Minnesota PUC concurred with the findings of an Administrative Law Judge ("ALJ") that Qwest had engaged in anti-competitive behavior, violating its interconnection agreement with AT&T and violating state and federal law. Qwest's actions demonstrate that it has no intention to cooperate with CLECs in testing and implementing competitive service offerings.

The facts of the adjudicated refusal of Qwest to provide required services are simple and quite telling.[387] AT&T informed Qwest that it intended to test UNE-P ordering and provisioning in Minneapolis ("Test Trial"). Despite months of meetings between the parties, Qwest at the eleventh hour flatly refused to conduct the Test Trial. Consequently, AT&T filed a complaint

[386] Arizona Report at 1; see also id. at 16 ("[P]rovisions in agreements which gave favored treatment in exchange for a party's agreement not to participate in proceedings before this Commission . . . are of extreme concern to the Commission and detrimental to the public interest").

[387] The recommended decision of Administrative Law Judge Mihalchick, for the Minnesota Public Utilities Commission, February 22, 2002, is Attachment 10 hereto. The recommended decision contains a detailed discussion of the facts of the case.

with the MPUC.[388] In addressing the AT&T's complaint on its merits, the ALJ concluded that Qwest committed a knowing, intentional, and material violation of its obligation to engage in cooperative testing under the Interconnection Agreement by its refusal to conduct AT&T's UNE-P test from September 14, 2000, to May 11, 2001. In his decision, the ALJ emphasized that Qwest's violations were knowing and intentional and constituted "a continuing pattern of conduct."[389] The ALJ also found that Qwest deliberately fabricated evidence in an attempt to assert that AT&T did not intend to enter the local exchange market in Minnesota.[390] These findings of the ALJ, left undisturbed by the full Commission, not only demonstrate an on-going pattern of anticompetitive behavior on the part of Qwest, but also show a willingness and ability on Qwest's part to violate Section 251, to prevaricate and to subvert the ability of a regulatory body to ensure that it will live up to its obligations in a competitive environment.

3. Qwest's Pervasive Violations of Section 271.

Qwest also clearly has engaged in a deliberate pattern and campaign of evading section 271, both before and after conditions were imposed on Qwest as part of its merger with U S WEST. The Commission has on three occasions adjudicated Qwest, and U S WEST before it, responsible for violating section 271. Qwest's penchant for prematurely entering the market for the provision of InterLATA services has not abated, because violations continue to this day.

Three FCC Adjudicated Violations. In at least three instances, Qwest and its predecessor U S WEST entered the interLATA long distance market in violation of section 271. First, the Commission addressed U S WEST's "teaming" arrangement with pre-merger Qwest and held

[388] On April 30, 2001, the Minnesota PUC issued an Order granting AT&T temporary relief requiring Qwest to complete certification and bill-conductivity testing. *In the Matter of the Complaint of AT&T Communications of the Midwest, Inc. against Qwest Corporation*, Docket No. P-421/C-01-391, Order Granting Temporary Relief and Notice and Order for Hearing, issued April 30, 2001 (Attachment 11 hereto).

[389] *See id.* at 34.

[390] *See id.* at 30-33; Minn. Stat. §237.121(a)(1).

that it violated section 271.[391] Under the "teaming" arrangement, U S WEST (and Ameritech) provided their local customers with a one-stop shopping opportunity that included interLATA services in violation of section 271.[392] Specifically, under the arrangement between U S WEST and Qwest, the incumbent local exchange carrier, among other things, (1) designed and developed a package of services that included long distance service, (2) selected and recommended Qwest as the long distance provider for the offering, (3) established and prospectively controlled the price, terms and conditions of the long distance offering, (4) served as the customer point of contact for the offering, and (5) marketed the offering under their brand.[393] In the face of these facts, the Commission concluded that:

> the business arrangements with Qwest permit Ameritech and U S WEST to provide in-region, interLATA services, prior to section 271 authorization. It is clear on this record that Ameritech's and U S WEST's business arrangements with Qwest pose the competitive concerns that section 271 seeks to address, and we accordingly find them unlawful under the Act.[394]

In the second proceeding, the Commission held that U S WEST's "provision of nonlocal directory assistance service to its in-region subscribers" constituted "the provision of in-region, interLATA service as defined in section 271(a) of the Act."[395] As the Commission recognized, the "nationwide component of U S WEST's nonlocal directory assistance service" was "unlawful" as it had been configured.[396] Once again, Qwest provided in-region, interLATA

[391] AT&T Corporation, et. al. v. U S West Communications, Inc., and Qwest Corporation, Memorandum Opinion And Order, 13 FCC Rcd 21438 (1998) ("Qwest Teaming Order") ¶ 52.

[392] *Id.* ¶¶ 1, 52.

[393] *Id.* ¶ 1.

[394] *Id.* ¶¶ 44, 52. The Commission noted that with the local market not yet open to competition, the results of offering local customers one-stop shopping were astoundingly anticompetitive. By leveraging its dominance in the local market to gain long distance customers, U S WEST persuaded *130,000* of its local customers to purchase Qwest's long distance service in just four weeks of marketing the unlawful one-stop shopping program.

[395] See Petitions of U S WEST Communications, Inc. for a Declaratory Ruling Regarding the Provision of National Directory Assistance; U S WEST Communications, Inc. for Forbearance, Memorandum Opinion and Order, 14 FCC Rcd 16252 (1999) ("NDA Order") ¶¶ 2, 63.

[396] *Id.* ¶ 63.

service without first demonstrating that its local markets were open to competition, without Commission approval, and in violation of Section 271.

Third, in February 2001, the Commission held that U S WEST's provision of a calling card platform that permitted its local subscribers to place long distance calls originating inside or outside of its local service area violated Section 271.[397] In finding that U S WEST intended to provide in-region, interLATA service, the Commission found that:

> U S WEST's participation in the long distance market through its 1-800-4USWEST Service enables it to obtain significant competitive advantages that are similar to what the *Qwest Teaming Order* found to be objectionable and almost identical to what the *1-800-AMERITECH Order* found to be objectionable. The Service allows U S West to build goodwill with its local-service customers, depicting itself as a full-service provider prior to receiving section 271 approval. Indeed, the full-service, or one-stop shopping, advantages provided by the Service appear to have been U S WEST's primary objective in implementing the Service in the first place. As the Commission held in the *1-800-AMERITECH Order,* these competitive advantages could reduce U S WEST's incentive to open its local market to competition and, thus, run counter to Congress's intent in enacting section 271.[398]

For the third time, the Commission found that Qwest had undertaken to provide interLATA services with the specific intent of undercutting the foundation of section 271.

Current Violation Of Section 271. While this pattern of past adjudicated violations of section 271 should cause ample Commission concern, Qwest's continuing violations of section 271 are even more troubling. Specifically, in violation of section 271 and the merger conditions that were imposed on Qwest's merger with US WEST (the "Merger"), Qwest continues to provide prohibited interLATA services. These violations are documented in proceedings that

[397] *AT&T Corporation v. U S WEST Communications, Inc.; MCI Telecommunications Corporation, Inc. v. U S WEST Communications, Inc.*, Memorandum Opinion and Order, 16 FCC Rcd 3574 (2001) ¶ 30.
[398] *Id.* ¶ 19.

surround audit reports filed by Qwest required by conditions on the Merger.[399] Qwest has employed three separate schemes, each of which is patently unlawful: it has used lit fiber capacity IRUs,[400] it has provided interLATA services to customers under the guise of "corporate communications,"[401] and, most brazenly, it has directly provided interLATA services "billed and *branded* as Qwest services."[402] As AT&T demonstrated in the audit proceedings following the Merger, the post-merger lit fiber capacity IRU arrangements neither were, nor could have been, approved in the *Qwest Merger Orders* and flatly violate section 271.[403]

In order to bring the Qwest-US WEST merger into compliance with Section 271, Qwest committed to divesting its interLATA operations in the US WEST region to an "independent" competitor, Touch America. The Commission accepted Qwest's and US WEST's representations that Touch America would not be dependent upon or controlled by Qwest and, therefore, that Qwest post-merger would not be "providing" interLATA services in violation of section 271. There is now substantial evidence that Qwest concealed a number of steps that it took to ensure that Touch America would remain dependent on Qwest in providing services to

[399] Two complaints also have been filed by Touch America, Inc. ("Touch America") against Qwest that relate to the violations documented in the audits filed pursuant to the Merger conditions. *See* Complaint, *Touch America, Inc. v. Qwest, Communications International, Inc.*, File No. EB-02-MD-003 (Feb. 2002) ("*IRU formal complaint*") and Complaint, *Touch America, Inc. v. Qwest, Communications International, Inc.*, File No. EB-02-MD-004 (Feb. 11, 2002) (revised and refiled March 1, 2002) ("*Divestiture formal complaint*").

[400] Letter from Arthur Anderson LLP to Dorothy Attwood (June 6, 2001), Finding 7 ("June 6, 2001 Supplemental Letter") (found with respect to 14 of 92 in-region service component codes sampled).

[401] *Id.*, Finding 2 (11 of the 458 account records were identified as providing prohibited in-region service in this manner).

[402] Report of Independent Accountants, Att. 1 at 1 (April 16, 2001) ("Initial Auditor's Report") (emphasis added); *see also id.* (for 266 customers with associated revenues from July 2000 through March 2001 in excess of $2.2 million); June 6, 2001 Supplemental Letter, Finding 9 (Qwest paid touch America only $856,863 out of $2,212,730 billed under for in-region interLATA services sold under Qwest's brand).

[403] Memorandum Opinion and Order, *Qwest Communications International Inc. and U S West, Inc. Applications for Transfer of Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License,* 15 FCC Rcd. 5376 (2000) ("March 10 Merger Order"); Memorandum Opinion and Order, *Qwest Communications International Inc. and U S West, Inc. Applications for Transfer of Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License*, 15 FCC Rcd. 11909 (2000) ("June 26 Merger Order") (collectively the "Qwest Merger Orders").

divested customers. Apparently, immediately after the "divestiture," Qwest undertook a concerted campaign to reacquire the most valued divested customers and to provide them (and others) with prohibited in-region interLATA services.

Specifically, although Qwest assured the Commission during the Merger proceedings that Touch America would be independent of Qwest when providing in-region interLATA service,[404] it plainly was not. Qwest, for example, assured the Commission that it would provide Touch America with sufficient access to Qwest databases so that it could support the in-region service customers being divested to it,[405] but as explained by Touch America, "Qwest has exercised such control over the data systems and software as to prevent Touch America from independently operating or servicing Transferred Customers."[406] Qwest similarly assured the Commission that under the Bilateral Wholesale Agreement, Touch America was not required to purchase out-of-region capacity on a wholesale basis from Qwest;[407] Touch America now says that Qwest's undisclosed billing system structure precluded Touch America from billing the transferred customers if it used a third party off-net provider for out-of-region capacity.[408] Qwest also represented to the Commission that it would lease to Touch America four circuit switches,[409] but Touch America has now disclosed that this did not occur and that Touch America was granted only limited functionality that did not provide it "with the kind of operational control over the

[404] *See, e.g.*, Qwest's Divestiture Compliance Report, at 18 (April 14, 2000) ("*April 14, 2000 Divestiture Plan*") (that under the Divestiture Plan "Qwest has further protected Touch America's ability to maintain a viable independent business within the region without restricting Touch America's ability to grow its business for national accounts"); *see also id.* at 12 ("Touch America is a strong and independent carrier that has the financial capacity and operational experience to provide excellent service to the customer base that Qwest will be divesting").

[405] *Id.* at 40-41.

[406] Divestiture formal complaint ¶ 193.

[407] "Point By Point Response To AT&T Comments On The Qwest Divestiture Compliance Report," Attachment A to Qwest's Reply Comments, at 20-21 (May 12, 2000) ("*Point By Point Response To AT&T Comments On The Qwest Divestiture Compliance Report*").

[408] Divestiture formal complaint ¶¶ 306-307.

[409] April 14, 2000 Divestiture Plan at 4, 19-20, 42.

switches that would allow Touch America to perform the 'core functions' associated with the operational management of a switch."[410] Just as significantly, Qwest did not disclose to the Commission its "lit fiber" "Indefeasible Rights of Use" ("IRUs") agreement with Touch America, although it contemplated the need for such an agreement even before it submitted its Divestiture Plan and began "negotiations" with Touch America weeks before the Commission issued its *Order* approving the Merger. Under this agreement, Touch America was required to pay Qwest for leasing interLATA network facilities *owned and operated by Qwest* in order to provide retail services to Touch America's "customers."

Qwest used these schemes as part of a winback strategy for large customers to replace private line services provided by Touch America. Thus, as set forth in Touch America's complaints, Qwest was able to reacquire Teleglobe, which was receiving leased line private line service from Touch America, by offering it lit fiber capacity IRUs.[411] Similarly, in March 1998 Qwest announced a 15-year pre-paid private line service arrangement with Verio.[412] Verio was then divested to Touch America and reacquired by Qwest with lit fiber capacity IRUs.[413] Touch America identified four other private line customers reacquired by Qwest using lit fiber capacity and alleges that a number of government accounts were also affected.[414]

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[410] Divestiture formal complaint ¶ 282; see generally id. ¶¶ 272-292.

[411] IRU formal complaint ¶¶ 75, 78.

[412] *See* Verio Form S-1/A filed on May 8, 1998, Exhibit 10.25, http://www.sec.gov/Archives/edgar/data/1040956/0000950134-98-003922.txt ("*Verio/Qwest Capacity Service Agreement*")

[413] IRU formal complaint ¶¶ 53-54.

[414] *Id.* ¶¶ 26-80. There is likewise considerable evidence that Qwest has been using in-region interLATA "corporate communications" in violation of Section 271. *Divestiture formal complaint* ¶¶ 338-40, 350-54, 431-46, 506. Touch America's complaints allege that Qwest has in fact been using its "corporate communications" to provide ordinary telecommunications services to unaffiliated third parties and that these services are not permissible Official Services or incidental interLATA services. All three audit reports filed by Qwest reveal that it has, in addition to these "stealth" in-region InterLATA services, also directly provided millions of dollars of *Qwest branded* in-region interLATA services and retained a substantial portion of the revenues from such services.

The Arizona InterLATA Gambit. As a final note on its anti-section 271 efforts, it must be recognized that Qwest's efforts began in Arizona, where US WEST attempted to make an "end-run" around the interLATA restrictions and provide long distance service there without opening its local market to competition. Specifically, Qwest sought to remove the LATA boundary within Arizona by asking that the ACC abolish the boundary. Once the LATA boundary was gone, Qwest believed it could provide telephone service throughout the state because such service would not be "interLATA service" within the prohibitions of Section 271.

The Commission was understandably quite concerned with these efforts to commit a "willful and knowing violation of the Act and the Commission's rules."[415] The Chief of the Commission's Common Carrier Bureau took the unusual course of writing to US WEST, stating the Commission's particular concern with expressions by US WEST representatives that the Commission lacked authority over in-state LATA boundaries and that US WEST could "provide telecommunications services across current LATA boundaries in Arizona without first applying to, and receiving approval from," the Commission for LATA boundary modifications. The Commission's concern rose to such a level that it required US WEST to provide a "written commitment" that it would not "begin to offer any telecommunications services across current LATA boundaries prior to receiving authority to do so from the FCC." In taking such an unusual step, the Commission appears to have been prescient with respect to Qwest/US WEST's propensity to compete in the provision of interLATA services without first opening its local exchange markets.

[415] Letter, June 1, 1999, from Lawrence E. Strickling, Chief, Common Carrier Bureau, to Mr. Bruce K Posey (Attachment 12 hereto).

4. Qwest's Other Anticompetitive Conduct

Freezing Service. Qwest has been ordered by the Iowa Board to cease its practice of freezing local service changes.[416] In response to a formal complaint filed by Cox Iowa Telecom, LLC ("Cox Iowa"), the Iowa Board investigated the need for Qwest's newly adopted policy freezing the switching of local service. The Board found only 14 confirmed cases of local slamming in Iowa in the one-year period that preceded Qwest's action, and concluded that given "the negligible state of local competition in Iowa and the few instances of local service slamming," the "local service freeze implemented by Qwest" at that time was "unnecessary to protect consumers" and would "have a detrimental effect on local competition."[417] Despite the action in Iowa, Qwest has maintained the policy of attempting to institute local service freezes in other states, and on March 29, 2002, AT&T was required to file a complaint with the Washington Utilities And Transportation Commission about Qwest's practice of adding local freezes to Qwest local service accounts.[418] As a result of Qwest's unilateral actions, customers were unable to switch to AT&T Broadband local service due to freezes on their accounts, even though the majority of customers asserted that they never authorized the freeze.

In fact, Qwest has a history of adopting anticompetitive freezes. In Colorado in February 1999, Qwest unilaterally extended PIC freezes (known as "jamming"). Qwest implemented this "PIC freeze extension" the day that intraLATA presubscription was implemented in Colorado – the first time that customers were able to choose their intraLATA carrier. Prior to intraLATA presubscription, and at the time that Qwest extended the preferred carrier freeze, customers in Qwest's service territory had no choice regarding the carrier that carried their intraLATA toll

[416] *Cox Iowa Telecom, LLC* v. *Qwest Corporation*, Docket No FCU-02-1, released April 3, 2002 (Attachment 13 hereto) at 9.
[417] *Id.* at 6, 8.
[418] *AT&T Corp. v. Qwest Corporation,* WUTC Docket UT-020388.

calls that were dialed direct from their line. All such calls were carried by Qwest. By extending the freeze to the intraLATA carrier, Qwest froze *itself* as the customers' carrier, thus negating the customers' ability to choose a carrier other than Qwest. Qwest rejected thousands of customers' orders to switch away from Qwest. AT&T, MCIWorldcom, and Nextlink all filed complaints regarding Qwest's action, and an ALJ found that the institution of the freeze violated Colorado law.[419] The Commission found that "USWC used its position as the sole 1+ intraLATA provider in its extensive service area to inhibit the entry of competitors into the intraLATA market and tangibly damaged the entering competitors."[420] The Commission also found that "USWC's abuse of its market position to inhibit and damage competition was anticompetitive."[421]

Inhibiting Entry. Qwest previously has denied AT&T access to inside wiring in multiple dwelling units ("MDUs), and in response to a complaint filed by AT&T, the WUTC, on April 9, 2001, ordered Qwest to promptly provide AT&T with access.[422] Qwest ripped out wires and conduit lawfully and properly installed by AT&T in various building access terminals located at the network interface device/minimum point of entry ("MPOE") terminals. Furthermore, Qwest padlocked boxes containing NID and other wiring, refused to negotiate access terms with AT&T and called the police when AT&T attempted to install its own wiring. Additionally, Qwest demanded non-viable, cost-prohibitive and commercially coercive methods for AT&T to obtain access to wiring inside the MDUs, such as insisting that such access required truck rolls by Qwest and that AT&T would have to reimburse Qwest its costs for each such truck roll. Such

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[419] *See Before the Public Utilities Commission of the State of Colorado,* Docket No. 99K-193T, Decision No. C00-301, March 22, 2000, citing Section 40-2-103. C/R/S/ as well as 4 *Code of Colorado Regulations* 723-25 ("Rule 25").

[420] *Id.* I.(E.)(2.).

[421] *Id.*

[422] *AT&T Communications of the Pacific Northwest, Inc.* v. *Qwest Corporation*, Docket No. UT-003120, Second Supplemental Order Granting Motion to Amend Answer, Denying Emergency Relief and Denying Motion for Summary Determination, issued April 9, 2001.

actions by Qwest in Washington and other states made it virtually impossible for AT&T to provide local residential service to customers located in MDUs.

Other CLECs, in various Qwest states, have raised similar issues concerning Qwest conduct that inhibits entry into the local exchange market. Some of these complaints have been withdrawn pursuant to confidential settlements that may involve agreements that should have been filed, but were not made public as required by Section 252. For example, SunWest Communications engaged in litigation with Qwest in August, October and November of 2000, alleging that Qwest, among other things, failed to provide interconnections in a timely manner. Qwest and SunWest entered into a confidential settlement of SunWest's complaint. Additionally, Rhythms Links, Inc., also filed a complaint against Qwest with the Colorado Public Service Commission regarding Qwest's discriminatory practices in offering ADSL-capable loops and ISDN-capable loops to CLECs.[423] In response and in settlement, Qwest began providing an ADSL-capable and an ISDN-capable loop to CLECs, but took nearly a year and impeded Rhythms' market entry throughout the Qwest region.[424] Scindo Networks similarly filed a complaint in Colorado, alleging that Qwest had repeatedly and intentionally violated the terms of its interconnection agreement on issues concerning collocation, dark fiber, and processing delays. Scindo Networks complained that Qwest's actions were intended to thwart competition from broadband competitors. According to a Stipulation for Dismissal, filed with the Commission on May 4. 2001, Qwest and Scindo Networks have entered into a confidential settlement regarding the complaint. Finally, in a ruling issued February 10, 1999, the WUTC

[423] *See Before the Public Utilities Commission For The State Of Colorado,* Rhythms Links Inc. (Complainant) v. U S West Communications, Inc. (Respondent), No. 99F-493T, October 7, 1999.

[424] Before the Public Service Commission of the State of Utah, *In the Matter of the Application of U S WEST Communications, Inc. For Approval Of Compliance With 47 USC § 271(d)(2)(B),* Docket No. 00-049-08, Affidavit of Valerie Kendricks, Rhythms Links, Inc., March 23, 2001, pp. 2-4.

found that Qwest-U S WEST had violated state laws and terms of its interconnection agreement by delaying MCI Metro from providing local phone service.[425]

In short, Qwest's pervasive efforts to avoid compliance with sections 251 and 252, when coupled with its past and ongoing violations of section 271, should provide the Commission with a strong conviction that Qwest is committed to entering the long distance market without committing itself to opening up its local markets. The Commission cannot be confident that Qwest will continue to open its local markets if the Commission grants this five-state Application.

C. Qwest Maintains Monopoly Power Over Residential Service.

Given the extensive pattern of Qwest noncompliance with the Act and its efforts to stall or prevent competition, it is not surprising that Qwest retains monopoly power over residential service in the five states covered by its application. In reviewing actual competition in the local market, the Commission reviews the extent to which new entrants "are actually offering" local service to both business and residential customers through each of the three means offered by the Act.[426] The "Act contemplates three paths of entry into the local market – the construction of new networks, the use of unbundled elements of the incumbent's network, and resale."[427] As the Commission has recognized, its public interest analysis "must include an assessment of whether all procompetitive entry strategies are available to new entrants."[428] And, as the Commission explained in the *Michigan 271 Order*, "[t]he most probative evidence that all entry strategies are

[425] *MCIMetro Access Transmission, Inc. v. U S WEST Communications, Inc.*, Docket No. UT-971063, Commission Decision and Final Order (Feb. 10, 1999). The WUTC found that U S WEST's practices imposed undue disadvantages on MCIMetro and granted unreasonable preferences to itself. Chairwoman Anne Levinson agreed with the majority opinion and also favored imposing substantial penalties against US WEST: "This is a consistent pattern of behaviors that all operated to U S WEST's advantage, gave it undue preferences, and subjected MCI to an undue competitive disadvantage and improper discrimination."

[426] Michigan 271 Order at ¶ 391.

[427] *Id.* ¶ 96.

[428] *Id.* at 387.

available would be that new entrants *are actually offering* competitive local telecommunications services to different classes of customers (residential and business) through a variety of arrangements (that is, through resale, unbundled elements, interconnection with the incumbent's network, or some combination thereof), in different geographic regions (urban, suburban, and rural) in the relevant state, and at different scales of operation (small and large)."[429] In subsequent applications, the Commission has repeatedly considered the degree to which competitors have actually succeeded in offering local telecommunications services using the different entry strategies prescribed by the Act.[430]

Here, Qwest's own data – particularly after Qwest's over-estimate of CLEC facilities-based lines is corrected -- confirm that facilities-based and UNE-based entry is extremely limited or non-existent in Qwest's service territories. Qwest relies on two methods to estimate facilities-based entry – one using E911 data, and a second using local interconnection service ("LIS") trunk data.[431] For four of the five states (all but Iowa), the trunk data estimate is lower than the estimate based on E911 data. However, it is clear that even Qwest's estimate based on trunk data is inflated. In order to estimate facilities-based lines served by CLECs, Qwest multiplies the number of LIS trunks by a factor of 2.75.[432] In support of the 2.75 factor, Qwest cites SBC's use of the same factor in SBC's 271 applications for Texas, Kansas and Oklahoma.[433] What Qwest fails to mention is that SBC's use of the 2.75 factor was flatly *rejected* by the Department of Justice as "much too high":

> "Although we believe it is reasonable to use the number of interconnection trunks in order to estimate the number of CLEC access lines, SBC's factor

[429] *Id.* ¶ 391 (emphasis added).

[430] *See, e.g., New York 271 Order* ¶¶ 13-14; *Texas 271 Order* ¶¶ 5-6.

[431] Teitzel Decl. ¶¶ 35-40.

[432] Teitzel Decl. ¶ 39.

[433] *Id.*

of 2.75 appears to be much too high. A more reasonable multiplier, in our view, would be close to one . . . ."[434]

Using the data presented by Qwest witness Teitzel – but using the "more reasonable multiplier" of one to estimate CLEC facilities-based lines, Tables 1 through 10 show the amount of CLEC competition in the five states.[435] The Tables show that less than 3% of all switched access lines in Idaho (Table 3), Idaho (Table 5) and North Dakota (Table 9) are served by facilities-based competitors (less than ½ of 1% in North Dakota). Similarly, less than 3% of all switched access lines are served by UNE-based competitors in Colorado (Table 1), Idaho (Table 3) and Nebraska (Table 7), with less than 1% in Nebraska. There is even less competition for residential service. A mere 465 lines, or 1/10 of 1% of the residential lines in Qwest's Idaho service territory, are served by facilities-based competitors, and only 126 lines, less than 1/10 of 1% of such lines, are served by UNE-based competitors (Table 4). Similarly, 485 lines, or less than ½ of 1% of the residential lines in Qwest's North Dakota service territory, are served by facilities-based competitors, and only 550 lines, again less than ½ of 1% of such lines, are served by UNE-based competitors (Table 10). In four of the five states, less than 1% of residential lines in Qwest's service territory are served by UNE-based competitors (the exception being Iowa, where a mere 2% of residential lines are served by UNE-based CLECs).

Furthermore, even these minuscule shares present an overly optimistic picture of the likely future of CLEC competition in the five states. As reflected in Attachment 15, many of the

[434] DOJ Texas Evaluation at n. 15 (February 14, 2000).

[435] According to the Tables (Attachment 14 hereto): In Colorado, facilities-based CLECs have 6.8% and 3.1%, UNE-based CLECs have 2.8% and 0.5%, and resale CLECs have 1.5% and 1.4% of the total and residential lines, respectively. In Idaho, facilities-based CLECs have 2.0% and 0.1%, UNE-based CLECs have 2.1% and 0.0%, and resale CLECs have 1.7% and 1.8% of the total and residential lines. In Iowa, facilities-based CLECs have 2.7% and 2.2%, UNE-based CLECs have 10.2% and 2.0%, and resale CLECs have 1.5% and 1.3% of the total and residential lines. In Nebraska, facilities-based CLECs have 7.6% and 6.6%, UNE-based CLECs have 0.9% and 0.4%, and resale CLECs have 2.4% and 2.3% of the total and residential lines. In North Dakota, facilities-based CLECs have 0.6% and 0.4%, UNE-based CLECs have 10.6% and 0.0%, and resale CLECs have 3.9% and 4.2% of the total and residential lines.

facilities-based CLECs identified as competitors by Qwest have gone, or are going, out of business, or are in severe financial distress at the present time.[436] The prospects for increased UNE-based competition are also bleak, because entry into residential service will be impaired so long as UNE rates remain above a level that permits competitive entry.

If Qwest actually offered CLECs non-discriminatory access to the full economies of scale in its network, the Commission would see meaningful entry and competition from UNE-based entrants.[437] The microscopic level of UNE-based entry in these states is by degrees of magnitude smaller than the level achieved in other states where the FCC has granted section 271 applications. As the Table below demonstrates, the current level of UNE-based competition for residential service in Idaho and North Dakota is *less than 1 percent* of the levels of UNE-based residential competition that existed in Massachusetts, New York and Pennsylvania at the time the Commission considered section 271 applications for those states.

ID and ND Versus Other States – CLEC Residential Entry Via Facilities and UNE-P

	Idaho	**North Dakota**	**NY**	**PA**	**MA**[438]
UNE-P	41	115	137,342	197,000	8,050 (approx)
Facilities	465	485	35,753	95,000	80,000 (approx.)
TOTAL	**506**	**600**	**173,095**	**292,000**	**88,050 (approx.)**

Finally, resale is an inherently limited competitive vehicle, both because resale-based competitors cannot alter the nature of the service they are reselling (and thus cannot provide

[436] *See also* Teitzel Decl., Exhibits DLT-Track A/PI-CO-4;.DLT-Track A/PI-ID-4; DLT-Track A/PI-IA-4; DLT-Track A/PI-NE-4; DLT-Track A/PI-ND-4.

[437] Since the passage of the Act, however, all CLECs combined in Idaho have managed to gain just 41 UNE-based residential lines, CLECs in North Dakota just 115 such lines, and Nebraska just 1,269 such lines.

[438] *New York 271 Order* ¶ 14: *Pennsylvania 271 Order* at n. 260; *Application of Verizon Pennsylvania Inc., et al. for Authorization To Provide In-Region, InterLATA Services in Pennsylvania*, FCC 01-269, at 52 (June 21, 2001); Comments of AT&T Corp., *Application of Verizon Pennsylvania Inc., et al. for Authorization To Provide In-Region, InterLATA Services in Pennsylvania,* CC Docket No. 01-138, at 71 (filed July 11, 2001) (citing to Qwest Witness Taylor, Att. 1, Exhibit B); *Application of Verizon New England Inc., et al. for Authorization to Provide In-Region, InterLATA Services in Massachusetts, Memorandum Opinion & Order,* CC Docket No. 01-09, ¶ 64 (September 22, 2000).

competitors with innovative or improved services), and because resale is priced in a manner that precludes its use in all but the most selectively chosen circumstances.[439] The record thus shows that resale is not a growing, viable source of future competition for Qwest in the five states, and that no entrant has yet succeeded in using either UNEs or facilities to offer competitive local residential service.

D. Qwest's UNE Rates Preclude UNE-Based Entry In Idaho, Iowa and North Dakota.

The evidence shows that Qwest's UNE rates, at least in Idaho, Iowa and North Dakota, are so high that they preclude efficient local entry. Specifically, those rates effect a price squeeze that prevents UNE-based competitors from earning sufficient margins to provide local service economically in competition with Qwest, by imposing wholesale costs on Qwest's competitors that render it impossible for them to offer a retail service that would be price competitive.[440]

Qwest's imposition of rates that foreclose broad-based local competition has two independent legal consequences in this proceeding. *First*, as described above, it establishes that those rates violate Checklist Item 2 because they are discriminatory. *Second*, the direct evidence of a price squeeze also establishes that granting the application could not be consistent with the "public interest." 47 U.S.C. § 271(d)(3)(C). The Commission has held that the "public interest" prong of Section 271 requires it to "ensure that no other relevant factors exist that would frustrate

[439] The avoided cost discount has proved inadequate to provide CLECs a basis for profitable entry for most consumers. For example, as monopolists, the incumbents do not face (and therefore do not "avoid") the huge customer acquisition costs that CLECs confront. Nor does avoided cost pricing take into account the lack of economies of scale that a new entrant must address. And CLECs providing resale do not benefit from access revenue. For all of these reasons, CLECs seeking to provide a broad-based, significant competitive alternative to the incumbents' local residential monopoly cannot do so through the resale of local service.

[440] *See* Lieberman Decl. ¶ 43.

the congressional intent that markets be open."[441] The central purpose of section 271 is to ensure that local telephone markets in a state are open to competition – and that competing carriers therefore have the legal and economic ability to provide competing local services – before a BOC in that state is permitted to provide long-distance services. A price squeeze that would foreclose efficient local entry into the residential market obviously constitutes such a "relevant factor." And proof that such a factor in fact exists demonstrates conclusively that the market is not – and cannot be – open.

The Commission nonetheless had previously held that it need not consider evidence of a price squeeze in evaluating a section 271 application. That holding was based on the Commission's view that such evidence was "irrelevant," and that considering it would improperly involve the Commission in the process of setting local retail rates that are outside its jurisdiction.[442] But the United States Court of Appeals for the D.C. Circuit, relying on the Supreme Court's decision in *Conway*, has now squarely rejected that view.[443] Indeed, because the central purpose of the 1996 Act is "stimulating competition," the D.C. Circuit held that the "public interest" analysis under section 271 may weigh even "*more heavily* towards addressing potential 'price squeeze'" than was required under the Federal Power Act in *Conway*.[444] Under

[441] *Kansas/Oklahoma 271 Order* ¶ 267. The Supreme Court has explained that the statutory term "public interest" "take[s] [its] meaning from the purposes of the regulatory legislation." *NAACP* v. *FPC*, 425 U.S. 662, 669 (1976). As the Commission has held, Congress adopted Section 271 in order to assure that BOCs could not provide long distance service at a time when their local monopolies would give them an "unfair advantage" over long distance competitors in, *inter alia*, providing "combined packages" of local and long distance service to customers who desire "one-stop shopping." *AT&T* v. *Ameritech*, 13 F.C.C. Rcd. 21438, ¶¶ 5, 39 (1998), *aff'd sub nom. U S WEST* v. *FCC*, 177 F.3d 1057 (D.C. Cir. 1999). If, by contrast, long-distance entry were allowed before other carriers could provide competing combined packages, it would "threaten competition" in both the local and the long-distance markets by granting the BOC a monopoly in the provision of such combined services. *Id.* ¶ 5.

[442] *Id.* ¶ 92.

[443] *Sprint* v. *FCC*, 274 F.3d 549 (D.C. Cir. 2001).

[444] *Id.* at 564 (emphasis added). Moreover, the *Sprint* Court also confirmed that the Commission's lack of jurisdiction over retail rates was no bar to such an analysis, because the Commission can respond to a price squeeze without disturbing retail rates. Instead, because the Commission has said that TELRIC rates exist within a "band," one entirely permissible solution is to "'fix[] the wholesale rates, which [a]re under its jurisdiction, at a lower level

Sprint v. *FCC*, therefore, when evidence is presented in a section 271 proceeding that UNE-based residential competition is economically infeasible, the Commission cannot grant that application without evaluating and addressing that evidence. Unless the Commission rejects this application on other grounds, it must develop and apply a framework for analyzing AT&T's claims.

In the face of the D.C. Circuit's *Sprint* decision, Qwest raises several arguments, none of which have merit. Qwest claims that it is legally irrelevant that UNE-P purchasers cannot economically provide service under Qwest's existing UNE rates. Qwest relies on antitrust cases that purportedly hold that a price squeeze can exist only if "essential inputs" are not available at a "fair price."[445] Qwest claims that this standard cannot be met here because UNE prices are necessarily "fair" if they have been found to fall within the range that satisfies TELRIC. Furthermore, Qwest claims that UNE-P is in no way an essential input in that the Act makes available resale under section 251(c)(4) and a variety of other means to gain access to Qwest's network.

Qwest's claims are baseless. As an initial matter, Qwest misstates the applicable antitrust decisions. For example, *Alcoa* holds that a firm with monopoly control over an input essential to the provision of a finished product is engaged in a price squeeze and is not charging a "fair" input price if purchasers of the input cannot make a "living profit" from sale of the finished product – as purchasers of UNEs plainly cannot in Idaho, Iowa and North Dakota.[446]

within'" that band. *Id.* at 564 (citing *Conway*, 426 U.S. at 279). Here, because, as AT&T has shown, Qwest's rates are not TELRIC-compliant to begin with, there is certainly plenty of room for downward movement.

[445] Application at 186, n. 124.

[446] *United States v. Aluminum Co. of America*, 148 F.2d 416, 436-38 (2d Cir. 1945). In *Town of Concord v. Boston Edison*, 915 F.2d 17 (1st Cir. 1990), the court only held that allegations that electric utilities have set wholesale rates to effect a price squeeze "generally" will not state claims under the antitrust laws because, among other things, the governing regulatory statute requires FERC to determine if a price squeeze will result at the time it reviews the lawfulness of the utility's wholesale rates. *Id.* at 28.

The antitrust decisions cited by Qwest are simply besides the point here for a similar reason. Whether or not Qwest is also violating antitrust standards, section 271 bars the Commission from granting Qwest long distance authority unless the Commission finds (1) that the UNE rates are "nondiscriminatory" as well as cost-based, 47 U.S.C. §§ 252(d)(1), 271(c)(2)(B)(ii) & (d)(3)(A)), and (2) that the grant of the application is in the "public interest." *Id.* § 271(d)(3)(C). As described above, in *Conway,* the Supreme Court has held that even if a utility's wholesale rates are within the range of reasonable cost-based rates, the rates are "discriminatory" and "anticompetitive" if they fall at the high end of that range and if they preclude wholesale purchasers from economically competing with the utility's retail services to any class of customers. Thus, if Qwest's high-end UNE rates foreclose UNE purchasers from economically providing residential competition, Qwest is engaged in "discrimination" and has not satisfied checklist item two. Because Section 271 categorically bars long distance authorization unless checklist item two has been "fully implemented," Qwest's arguments about the availability of resale or other means of access are irrelevant in this context.

Qwest's reliance on the purported availability of resale to respond to evidence that its high UNE prices have doomed UNE-based competitors to failure is also unavailing in the public interest context. To begin with, resale is irrelevant for this purpose. The wholesale discount that has been set in Idaho, Iowa and North Dakota is wholly insufficient to allow any firm to cover its internal costs of service, and no firm could economically provide local exchange service in these states through resale on a broad basis over time.[447] This is borne out by the paltry market shares currently enjoyed by resale-based competitors in Idaho, Iowa and North Dakota.

[447] Most notably, a competitor that provides services using resale is not entitled to receive either USF support or access revenues. Thus, its potential revenues are significantly reduced compared to providers that employ UNE-P.

More fundamentally, resale would be irrelevant even if the wholesale discount that has been set in these states was sufficient, for resale does not give a CLEC access to the "inputs" required to provide long distance service. In particular, firms engaged in resale are entitled to use the BOCs' facilities to provide only exchange service and not exchange access service. Resale thus has no effect on the BOCs' monopoly over the exchange access services that originate and terminate all long distance calls, and resale cannot eliminate a BOC's ability to leverage its monopoly into the long distance market.

Nor is there any other entry vehicle that is available to AT&T and other CLECs in Idaho, Iowa and North Dakota that could allow multiple CLECs to provide residential service throughout the state. As shown above, facilities-based providers serve less than ½ of 1% of residential access lines in Idaho and North Dakota and only about 2% in Iowa. Under these circumstances, the only theoretical alternative to UNE-P would be an arrangement in which firms would attempt to provide residential service by leasing unbundled loops from Qwest and combining them with the CLECs' switches to provide service. However, such a "UNE-L" strategy is now wholly uneconomic for this purpose in these states (and elsewhere). Quite apart from the fact that carriers cannot rationally invest in switches until they have used UNE-P to build up a customer base, Qwest and other BOCs have not deployed technology that allows customers to change from one local exchange carrier to another efficiently and effectively, in mass market quantities and at low cost. Instead, these changes require manual "hot cuts" which are expensive and which have proven impossible for Qwest and other BOCs to administer without causing unacceptable levels of service outages even when UNE-L is used only for low volumes of orders for business customers.[448]

[448] Finally, Qwest points to the Commission's decisions in the *Vermont 271 Order* and the *Georgia/Louisiana 271 Order*. Br. 187-88. However, these prior Commission decisions on the price squeeze issues were based on the

In sum, the lack of facilities- and UNE-based CLEC competition for service in the five states is due to Qwest's "failure to cooperate in opening its network to competitors" and the "existence of barriers to entry," *not* "the business decisions of potential entrants" that are independent of the entry barriers and BOC misconduct.[449] Nothing suggests that potential entrants have decided that the local markets in these five states, though open, are simply not worth pursuing, or "that competitive alternatives can flourish rapidly throughout the state."[450] The local markets in the five states are simply not open to competition, let alone irretrievably open.

E. Qwest's Performance Remedy Plans Are Inadequate To Demonstrate 271 Compliance.

The current record provides no basis for Qwest's claims that its performance enforcement plans will serve as effective deterrents against future backsliding.

There is no factual basis for Qwest's claims that its performance remedy plans contain a comprehensive set of self-executing remedies demonstrating that it will continue to provide CLECs with nondiscriminatory service in the wake of any Section 271 relief. Performance monitoring and enforcement mechanisms can "constitute probative evidence that the BOC will continue to meet its Section 271 obligations and that its entry would be consistent with the public

records in those proceedings. As explained above, the record concerning Qwest's price squeeze here fully meets the standards for establishing a price squeeze that the Commission has identified in prior cases. The *Vermont 271 Order* (¶ 67) suggests that *Conway* may be inapplicable in this context. As *Sprint* v. *FCC* makes clear, however, the court that reviews the Commission's section 271 decisions disagrees. In any event, the suggested distinctions are specious. Establishing that UNEs, unlike the electricity at issue in *Conway*, have prices that may "vary by location" and are not "undifferentiated commodities" might impact the estimation of margins, but not the applicability of the legal rule that where a price squeeze is demonstrated, wholesale rates are discriminatory and contrary to the public interest. Nor is it relevant that "intentional state policy" may have caused wholesale rates to exceed retail rates; AT&T does not ask the Commission to interfere with (or even comment upon) state policy, but merely to determine whether a price squeeze exists and, if so, whether it would serve the public interest to grant a section application. And, as AT&T has repeatedly shown, and repeats here, resale requirements do not solve the price squeeze because, *inter alia*, the wholesale discounts available are also too small to allow profitable entry.

[449] *Michigan 271 Order* ¶ 391.

[450] *Id.* ¶ 392.

interest."[451] But the Commission has made clear that, when an applicant relies on a performance monitoring and enforcement plan to support its application, it will review the contours of that plan to assess whether it provides sufficient incentives for compliance with Section 271, stating:

> Where, as here, a BOC relies on performance monitoring and enforcement mechanisms to provide assurance that it will continue to maintain market-opening performance after receiving Section 271 authorization, *we will review the mechanisms involved to ensure that they are likely to perform as promised. While the details of such mechanisms developed at the state level may vary widely, we believe that we should examine certain key aspects of these plans to determine whether they fall within a zone of reasonableness, and are likely to provide incentives that are sufficient to foster post-entry checklist compliance.*[452]

Moreover, the Commission has identified certain key elements in a legitimate performance monitoring and enforcement plan. Thus, in the *New York 271 Order*, the Commission endorsed the New York performance assurance plan because it contained the following characteristics: (1) potential liability that provides a meaningful and significant incentive to comply with the designated performance standards; (2) clearly-articulated, pre-determined measures and standards, which encompass a comprehensive range of carrier-to-carrier performance; (3) a reasonable structure that is designed to detect and sanction poor performance when it occurs; (4) a self-executing mechanism that does not leave the door open unreasonably to litigation and appeal; and (5) a reasonable assurances that the reported data is accurate.[453]

Similarly, in its subsequent decisions reviewing Section 271 applications, the Commission has evaluated each performance remedy plan at issue based upon these same

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[451] *New York 271 Order* ¶ 429. *See also Massachusetts 271 Order* ¶ 236; *Kansas/Oklahoma 271 Order* ¶ 273.

[452] *New York 271 Order* ¶ 433 (emphasis added). See also *Texas 271 Order* ¶ 423; *Kansas/Oklahoma 271 Order* ¶ 273.

[453] *New York 271 Order* ¶ 433.

characteristics.[454] Qwest's performance monitoring and enforcement mechanisms do not and cannot satisfy these criteria.

No anti-backsliding plan can be effective unless it is based upon a system of comprehensive and performance measurements producing accurate and reliable performance results that are coupled with enforcement mechanisms that can effectively deter Qwest from engaging in anticompetitive conduct. These conditions do not presently exist.

In this regard, the performance remedy plans on which Qwest relies are fundamentally flawed because Qwest's performance data that serve as the basis for the calculation of remedies payments are inaccurate and untrustworthy. Because the performance data which serve as the springboard for remedies payments are inaccurate, they fatally compromise the efficacy of the performance remedy plans. Even if Qwest's data were accurate, reliable and comprehensive – and they are not – the very structure of Qwest's remedy plans render them ineffective tools to deter anticompetitive conduct after any section 271 entry.

Contrary to Qwest's claim, the performance remedy plans are flawed in both their comprehensiveness and ability to capture actual performance. The performance remedy plans cannot possibly capture Qwest's actual performance because they omit measures that are necessary to detect discriminatory performance. The omitted metrics – which include measures on service order accuracy and functional acknowledgments – are neither trivial nor insignificant. Because the current performance remedy plans exclude these measures, Qwest will suffer no financial consequences for plainly discriminatory conduct.

Aside from these deficiencies, other provisions in Qwest's performance enforcement plans fail to provide sufficient incentives to assure that Qwest will fulfill its statutory obligations.

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[454] *See Texas 271 Order* ¶¶ 424-429; *Kansas/Oklahoma 271* Order ¶¶ 273-278; *Massachusetts 271 Order* ¶¶ 240-247; *Connecticut 271 Order* ¶¶ 76, 77.

In that connection, in every proceeding in which Section 271 approval has been granted, the Commission has found that the performance remedy plan adopted by the State commission was not "the only means of assuring that [the BOC] continues to provide nondiscriminatory service to competing carriers."[455] In these proceedings the Commission found that the BOC applicant "faces other consequences if it fails to sustain a high level of service to competing carriers, including: "federal enforcement action pursuant to Section 271(d)(6), liquidated damages under dozens of interconnection agreements, and remedies associated with antitrust and other legal actions."[456] However, the performance enforcement plan approved by the Idaho Public Utilities Commission *precludes* CLECs from obtaining such alternative forms of relief and is plainly contrary to this Commission's well-established precedent.

Similarly, this Commission has recognized the important role that state regulatory agencies must play in monitoring and enforcing a BOC's compliance with its statutory obligations after Section 271 relief is granted. Indeed, this Commission has emphasized that "state performance monitoring and post-entry enforcement"[457] mechanisms are "critical complements to the Commission's authority to preserve checklist compliance pursuant to section 271(d)(6)."[458]

In approving Bell Atlantic's New York 271 application, the Commission emphasized that the New York PSC was "committed to supervising the implementation of [performance assurance] plans" that were designed to assure that the markets remained open in the wake of

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[455] *Texas 271 Order* ¶ 424. *See also New York 271 Order* ¶ 430; *Georgia/Louisiana 271 Order* ¶ 296.

[456] *Texas 271 Order* ¶ 424. *See also New York 271 Order* ¶ 435; *Pennsylvania 271 Order* ¶ 130 n. 448; *Georgia/Louisiana 271 Order* ¶ 296.

[457] *Texas 271 Order* ¶ 420, n.1219 (emphasis added); *New York 271 Order* ¶ 429, n. 1316; *Kansas/Oklahoma 271 Order* ¶ 269, n. 828; *Massachusetts 271 Order*, ¶ 236, n. 757.

[458] *Texas 271 Order* ¶ 420.

Section 271 relief.[459] Because of the vital role that the New York PSC played and would continue to play in monitoring and adjusting the performance monitoring and remedy plan as needed, this Commission was confident that the New York monitoring and enforcement plan would be revised as needed "to reflect changes in the telecommunications industry and in the New York market."[460]

However, the Iowa performance remedy plan – which explicitly permits Qwest to challenge the authority of the State to make any changes to the plan – poses a significant risk that CLECs will be faced with protracted litigation whenever the State imposes a change that is not to Qwest's liking. If Qwest is free to challenge the authority of the State to make changes to the plan, Qwest could render the plan a static document that would never evolve at a pace that is consistent with the dynamics in the telecommunications market.

Qwest simply cannot have it both ways. Qwest should not be permitted to rely on a remedy plan for 271 approval, while simultaneously reserving the right to challenge the authority of the state to make any changes to that plan. Moreover, the reservation of such rights undermines the Commission's stated goal of having "self-executing enforcement mechanisms that are automatically triggered by noncompliance with the applicable performance standard without resort to lengthy regulatory or judicial intervention."[461] For all of these reasons, Qwest's performance enforcement plans cannot possibly meet the public interest requirements under Section 271.

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[459] *New York 271 Order* ¶ 12.

[460] *Id.*

[461] *Michigan 271 Order* ¶ 394.

CONCLUSION

For the foregoing reasons, Qwest's application for authorization to provide in-region, interLATA services in Colorado, Idaho, Iowa, Nebraska, and North Dakota should be denied.

Respectfully submitted,

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July 3, 2002

CERTIFICATE OF SERVICE

I hereby certify that on this 3d day of July, 2002, I caused true and correct copies of the forgoing Reply Comments of AT&T Corp. to be served on all parties by mailing, postage prepaid to their addresses listed on the attached service list.

Dated: July 3, 2002
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/s/ Peter Andros

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